In The

Supreme Court of the United States

October Term, 1978

No. 79-366

ARGENTINE AIRLINES,

Petitioner,

vs.

PHILIP ROSS, as Industrial Commissioner of the State of New York,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE STATE OF NEW YORK COURT OF APPEALS

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In The

Supreme Court of the United States

October Term, 1978

No.

ARGENTINE AIRLINES,

Petitioner,

vs.

PHILIP ROSS, as Industrial Commissioner of the State of New York,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE STATE OF NEW YORK COURT OF APPEALS

To the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioner, Argentine Airlines, hereby petitions for a writ of certiorari to review the decision of the New York Court of Appeals entered in this proceeding on June 5, 1979.

OPINION BELOW

The opinion of the Supreme Court of the State of New York, Appellate Division for the Third Judicial Department, reported at 64 App. Div. 2d 994, 408 N.Y.S.2d 831, N.Y.

Unempl. Ins. Rep. (CCH) ¶10,736, appears in the Appendix hereto. The opinions of the Unemployment Insurance Appeals Board of the State of New York, unreported, also appear in the Appendix.

JURISDICTION

The order of the Appellate Division, Third Department, was made and entered on October 2, 1978. A timely motion for reargument or, in the alternative, leave to appeal to the Court of Appeals of the State of New York was denied by the Appellate Division by order entered on March 8, 1979. A timely motion for leave to appeal to the Court of Appeals of the State of New York was denied by that court on June 5, 1979, and the present petition was filed within 90 days of that date, as enlarged to 91 days pursuant to Supreme Court Rule 34, the 90th day being Labor Day, a legal holiday. This Court's jurisdiction is invoked under 28 U.S.C. §1257(3).

QUESTION PRESENTED

Whether it is an abuse of discretion and as such a denial of due process under the Fourteenth Amendment for a state to promulgate a rule retroactively assessing unemployment insurance tax against a foreign airline for a period when the state, by prior consistent application of a statute, denied the burdens and benefits of unemployment insurance to this petitioner and similar foreign airlines and their employees.

STATEMENT OF THE CASE

After over two decades of excluding Argentine Airlines from the unemployment insurance fund, New York State has retroactively assessed unemployment insurance premiums against the airline for 1971, a time when it and its employees were ineligible for the benefits of the program.

In 1971, petitioner Argentine Airlines (otherwise known as "Aerolineas Argentinas") operated as an arm of the national government of the Republic of Argentina. It was neither a corporation nor an instrumentality of the government of Argentina, but the government itself.

From the time Argentine Airlines first flew to New York in the late 1940's, and through 1971, the State of New York considered the airline ineligible to contribute to the New York State Unemployment Insurance Fund and its employees were ineligible to receive unemployment insurance benefits. When the airline requested to voluntarily participate in New York's program, it was informed that it could not because, as a foreign government, Argentine Airlines was excluded from participation by §560(4) of New York State's Labor Law as it existed until January 1, 1978: "Governmental organizations. Municipal corporations and other governmental subdivisions shall not be employers liable for contributions under this article." N.Y. Lab. L. §560(4) (McKinney 1977).

The airline, as a foreign government, also fell outside the pre-1978 statutory definition of a qualified "employer."[1]

The exclusion of Argentine Airlines and its employees was consistent with the treatment of other foreign government airlines by the Industrial Commissioner of New York. Irish International Airlines contributed to New York's unemployment fund until 1965 when the Industrial Commissioner of his own volition decided that under §560(4) Irish Airlines was not an

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1. N.Y. Lab. L. §512 (McKinney 1977):

> "'Employer' includes the state of New York and any person, partnership, firm, association, public or private, domestic or foreign corporation, the legal representatives of a deceased person, or the receiver, trustee, or successor of a person, partnership, firm, association, public or private, domestic or foreign corporation."

eligible employer because it was owned by a foreign government. Irish Airlines' request to contribute voluntarily was turned down, as were the claims of a number of Irish Airlines' former employees. The decision of Department of Labor Referee Arthur Mendelson, filed on December 11, 1968, which upheld the determination to deny benefits to Donald Saunders, a former employee of Irish Airlines, states:

> "OPINION: Section 560(4) provides that governmental subdivisions are not employers liable for contributions under the New York Unemployment Insurance Law. Irish International Airlines is a governmental subdivision and, therefore, claimaint cannot be credited with his employment with this carrier. It follows that the initial determination ruling him ineligible was correctly issued and must be sustained."

Donald Sauders, No. 81-147-68 (N.Y. Unempl. Ins. Referee Sec., Dec. 11, 1968).

Lan-Chile, the Chilean government-owned airline, had also been ruled exempt from the Unemployment Insurance Law, only to have the Commissioner later overturn that ruling: "Until July 1972, it [Lan-Chile] was considered not subject to the Law because of its deemed status as a foreign government instrumentality." *Lan-Chilean Int'l Airlines,* No. 34304-72 (N.Y. Unempl. Ins. Referee Sec., Dec. 12, 1972), *aff'd,* No. 180, 734 (N.Y. Unempl. Ins. App. Bd., Mar. 7, 1973).

By virtue of its governmental status, Argentine Airlines had also been exempted from various federal and state taxes including Federal Unemployment Tax, Federal Insurance Contributions Tax, Federal Withholding, Florida Unemployment Tax, United States Income Tax and New York State and City Sales Tax.

As a direct result of the Industrial Commissioner's refusal to allow Argentine Airlines to voluntarily participate in New York's unemployment insurance program, the airline was required by its union, Transport Workers Union, Airline Division, to furnish its employees with an alternative to unemployment insurance. A system requiring large severance payments of up to eleven weeks' salary was substituted for unemployment insurance and it was understood by the airline and its employees that the employees were not eligible for New York unemployment benefits.

The review of Argentine Airlines' status was precipitated by the first claim filed by a former employee for unemployment benefits and resulted in the December 30, 1974 Industrial Commissioner's determination which held that the airline was, after all, liable for contributions to New York's unemployment fund. The Industrial Commissioner has therefore retroactively assessed the airline for contributions from January 1, 1971 onward. Similarly, retroactive review of the prior ineligible status of the foreign airline was precipitated by the filing of an initial claim after the affected period in the *Lan-Chile* case. *E.g., In re Irish Int'l Airlines,* 41 N.Y.2d 819, 393 N.Y.S.2d 397, 361 N.E.2d 1045 (1977), *mem. aff'g* 48 App. Div. 2d 202, 369 N.Y.S.2d 24 (3d Dep't 1975), *aff'g* No. 183, 789 (N.Y. Unempl. Ins. Appeals Bd., Feb. 8, 1974).

The effect of the Industrial Commissioner's action with regard to Argentine Airlines was to rewrite the accepted and long-applied interpretation of New York Labor Law §560(4) (McKinney 1977). The specific language of a §560(4) was in effect since 1935 and had, along with §512, been interpreted consistently by the Commissioner for over 45 years to exclude foreign governments from the unemployment program. The Commissioner's action against petitioner rewrote long-settled law to include a foreign government as a covered employer. This is the type of statutory change which can be accomplished only by legislation. It was precisely that kind of legislation which was

enacted by the New York State Legislature effective January 1, 1978: When New York Labor Law §560(4) which had excluded foreign government employers was repealed, the definition of eligible "employer" in §512 was simultaneously amended to include "and other governmental entities", and §565 was added, reading: as eligible employers, "A governmental entity shall mean the state of New York, municipal corporations and other governmental subdivision [*sic*] and any instrumentality of one or more of the foregoing." Act of Aug. 3, 1977, Ch. 675, §§4, 6, 11, 1977 N.Y. Sess. Laws 1025 (McKinney).

The Commissioner's determination in Argentine Airlines case was affirmed by a Labor Department referee on January 16, 1976, the referee's decision was modified and affirmed by the Unemployment Insurance Appeals Board on January 25, 1977, and the Appeals Board decision was affirmed by the Appellate Division on September 21, 1978. On February 2, 1979 the Appellate Division denied permission to reargue or appeal to the Court of Appeals and on June 5, 1979 the Court of Appeals denied permission to appeal.

The constitutional question herein was raised in the appeal filed in the Appellate Division of the Supreme Court of New York, Third Department, to review the decision of the Appeals Board assessing liability. The question was specifically raised in Point IV of the brief on appeal: "[T]o impose liability on Aerolineas retroactive to January 1, 1971 would be grossly inequitable and unconstitutional."

Referring to *Central Illinois Public Service Co. v. United States*, 435 U.S. 21 (1978) (where this Court voided a retroactive assessment against an employer for failure to withhold income tax on the value of a company-furnished lunch which had recently been declared as compensation to the employee), your petitioner argued that the constitutional ruling there made[2]

2. "[W]here an employer had no reason to know he should have paid a tax, then in the absence of express statutory authority, a retroactive assessment could not be made."

"applies also to a state assessment." The constitutional issue was again raised in both the motion for reargument to the Appellate Division and in the motion for the Court of Appeals: "Was it a denial of due process for the Industrial Commissioner to assess New York Unemployment Insurance Taxes against Appellant retroactively?"

Neither the Appellate Division nor the Court of Appeals expressly passed upon this constitutional issue; however, these courts could not have affirmed the decision below without resolving the constitutional question against the petitioner. *Chicago Life Ins. Co. v. Needles*, 113 U.S. 574, 579 (1885).

REASONS FOR GRANTING THE WRIT

In *Central Illinois Public Service Co. v. United States*, 435 U.S. 21 (1978), this Court recently addressed the situation where an administrative agency uses its adjudicatory power retroactively in order to effect a change in the application of a statute to a larger body of taxpayers. Petitioner respectfully submits that *Central Illinois* bears directly on the instant case, as the Industrial Commissioner used the determination against petitioner as the means to redefine the unemployment insurance liability of a foreign government airline. Petitioner maintains that this is the type of statutory change which cannot be properly made with the adjudicatory power of an administrative agency. *Central Illinois* was brought to the attention of the New York Supreme Court, Appellate Division—Third Department in appellant's brief. The Appellate Division did not speak to the issues raised by *Central Illinois* when it affirmed the Appeals Board decision.

By refusing to review the Appellate Division's decision, the New York State Court of Appeals in effect refused to apply *Central Illinois* to the instant case. It is petitioner's brief that the principles of *Central Illinois* are controlling in this case and that it was error for New York State's appellate courts to ignore the leading Supreme Court case on point.

Central Illinois discussed two levels of inquiry in situations involving administrative adjudications having retroactive effect, both being pertinent to the case at bar. One question which must be answered when reviewing an administrative adjudication is whether or not the agency had the authority to make the change in interpretation of law it announced in the decision by adjudication, or whether such a change in law would be better left to a prospective ruling by the agency or to the Legislature itself. In *Central Illinois,* this Court held that it was not appropriate for the Internal Revenue Service to apply law defining income subject to personal income tax, to employers' withholding liability in an adjudication, for to do so would effect a substantial change in the law which is not within the Service's adjudicatory authority.

A similar situation exists in the instant case where the Industrial Commissioner changed the definition of eligible "employer" under New York's unemployment insurance law by ruling against petitioner and the two other foreign airlines in claims hearings. This redefinition rests exclusively with the New York State Legislature, which properly asserted its authority with the changes in this law which it made effective January 1, 1978.

Assuming *arguendo* it was proper for the Industrial Commissioner to change the definition of eligible "employer" for unemployment insurance purposes by adjudication, the question still remains as to whether or not application of this change is an abuse of discretion and as such a denial of due process.

Argentine Airlines did not pattern its conduct on its own interpretation of unsettled law or on gratuitously offered advice from the agency or similar-appearing decisions of the agency or even a favorable ruling of the agency sought by the airlines, but rather it relied on a decision by the Industrial Commissioner against its request to voluntarily contribute to the unemployment fund. Argentine Airlines did not search New

York labor law for a loophold to exclude it from contribution to the unemployment fund, nor did the airline approach the Industrial Commissioner with a theory of interpretation of N.Y. Labor Law §560(4). It is the Industrial Commissioner who answered the airline's request for voluntary contribution with the Department of Labor's interpretation of §560(4) and the Industrial Commissioner who consistently asserted that interpretation for over two decades. Assuming *arguendo* that the Industrial Commissioner has the authority to change this interpretation, petitioner submits it is capricious and arbitrary to do so retroactively.

Argentine Airlines' reliance on the Industrial Commissioner's adamant refusal to allow the airline to participate in the unemployment program was great. The severance payment clause negotiated by the Transport Workers Union as an alternative for unemployment insurance cannot be removed from the contract now that the Industrial Commissioner has decided unemployment insurance must now be paid. Any attempt to remove these excessive payments from future payments would be viewed by the union as a reduction of benefits and would have to be compensated for by Argentine Airlines. In reality, the flip-flop performed by the Commissioner on the issue of Argentine Airlines' eligibility will cause the airline to pay for double unemployment coverage far into the future.

While Argentine Airlines pays twice for unemployment coverage during the retroactive period, the unemployment insurance fund is unjustly enriched by the contributions assessed for that time. Because the airline's employees were not eligible for benefits in the retroactive period the airline is being required to pay the unemployment insurance fund for coverage of a risk the fund did not insure.

When the Industrial Commissioner decided that a former employee of Argentine Airlines was eligible for unemployment benefits, he was faced with the question of when the airline's

liability for the insurance to pay for these benefits began. The Commissioner did not assess liability back to the date when this employee was hired, or in an amount calculated to cover the benefits this claimant could expect to collect, or any other rational basis keyed into the cost to the insurance fund or the benefit to the airline. Instead, the Industrial Commissioner extended his arm as far as the statute of limitations would allow him. Without any showing of bad faith on the part of the airline, this retroactive assessment can only be seen as grossly punitive, capricious, and arbitrary.

Petitioner respectfully submits that the retroactive assessment in the instant case constitutes an abuse of discretion which violates the due process clause of the Fourteenth Amendment.

> "It is well established that the states have wide discretion in the laying and collecting of their taxes. The law is equally clear, however, that such discretion cannot be exercised so as to arbitrarily deprive persons of their constitutional rights. So, while the Fourteenth Amendment does not require precise equality or uniformity in taxation, or prohibit inequality in taxation which results from mere mistake or error in judgment of tax officials, it does 'secure every person within the state's jurisdiction against intentional and arbitrary discrimination, whether occasioned by express terms of a statute or by its improper execution through duly constituted agents.' Stated differently, the Fourteenth Amendment protects only against taxation which is palpably arbitrary or grossly unequal in its application to the persons concerned."

Weissinger v. Boswell, 330 F. Supp. 615, 621-22 (N.D. Ala. 1971) (footnotes omitted).

The retroactive assessment charged against Argentine Airlines was not only arbitrary, but had the effect of requiring the airline to pay for unemployment coverage twice, unlike other taxpayers who were either included or exempted from New York State's unemployment insurance program, rather than both at the same time. Moreover, here, as in the cases reviewed in *Milliken v. United States*, 283 U.S. 15, 21 (1931),

> "the nature and amount of the tax burden imposed could not have been understood and foreseen by the taxpayer at the time of the particular voluntary act which was made the occasion of the tax."

In petitioner's case, the unforeseeability lay not in the existence of the unemployment insurance tax, but in its application to petitioner in the absence of statutory authority and contrary to past administrative interpretation.

A strikingly similar due process violation was found in the review of criminal convictions in *Bouie v. City of Columbia*, 378 U.S. 347 (1964). There, a criminal trespass statute was consistently construed for 95 years not to prohibit Bouie's conduct; yet his conviction was affirmed by the state court upon the basis of a seemingly unwarranted construction of the law in another recent case. 378 U.S. at 352, 356-57. Here, the definition of who would be liable for the tax was consistently held to exclude foreign governments or their agents for at least 35 years; yet the airline was held liable retroactively on the basis of the *Irish Airlines* case. In *Bouie*, the gap in the law "filled" by the unwarranted judicial construction was subsequently and prospectively covered by legislation. *See* 378 U.S. at 359 n. 7. New York's enactment of Labor Law §565 (McKinney Supp. 1978-79) furnished an exact parallel.

Petitioner respectfully submits that had the New York State courts applied *Central Illinois* to the instant case, as the Seventh

Circuit did in *Crown v. Commissioner*, 585 F.2d 234 (7th Cir. 1978), the constitutional violations would have been cured. In *Crown*, the Commissioner of Internal Revenue attempted to apply statutory language which had been in existence for some time in such a way as to redefine a loan previously considered non-taxable as a taxable gift. The *Crown* court recognized that the Commissioner was using this determination, which because of its retroactivity had a grossly inequitable effect on the taxpayer, to promulgate a new rule concerning interest-free loans.

The *Crown* decision cited *Central Illinois* when discussing why the retroactive application of this newly announced rule would have an inequitable effect on the taxpayer. The *Crown* decision further applied the philosophy of *Central Illinois* when it held that the Commissioner may not use his adjudicatory power to promulgate new rules: "In conclusion, although we are sympathetic to the Commissioner's desire to fill in what may be a significant loophole in the gift tax laws, a number of theoretical and practical problems make it undesirable to do so by judicial construction." *Id.* at 241.

The *Crown* court has taken the principles of *Central Illinois*, particularly Justice Brennan's concurring opinion which dealt with retroactivity, and has given them general application beyond the area of withholding tax. In *Crown*, as in the instant case, the Commissioner was not simply bringing the taxpayer in line with other similarly situated taxpayers, but was developing new law for an entire class of taxpayers. As *Crown* further pointed out, if the authority to create this new law rests with the Commissioner at all, rather than the Legislature, it is by prospective regulation, not retroactive adjudication. *See id.* at 241.

Other circuits have not been as quick to apply the general principles of *Central Illinois* as the Seventh Circuit. As a result, a conflict exists among the circuits in this area. In *Benedict Oil*

Co. v. United States, 582 F.2d 544 (10th Cir. 1978), the Tenth Circuit decided a case involving the question of the taxable status of expenses attributable to the sale of corporate assets during a liquidation. The taxpayer asked the court to apply a circuit court decision that had been handed down when the taxpayer applied for a refund, and not subsequent decisions which overruled the earlier decision beneficial to the taxpayer. In refusing to apply the later decisions prospectively only, the *Benedict* court relied heavily on *Dixon v. United States*, 381 U.S. 68 (1965), which held that the Internal Revenue Service is allowed wide discretion in retroactive adjudication. It appears that the *Benedict* court ignored the modifying effect of *Central Illinois:* "We are cited no decision of the United States Supreme Court or of the courts of appeals, nor have we found any, which gave prospective effect only when an income tax decision was overruled." 582 F.2d at 549. It appears that either the *Benedict* court was unaware of the *Central Illinois* decision or construed its holding so narrowly that it could not see the application in *Benedict*.

Petitioner respectfully submits that *Central Illinois* is a clarification of *Dixon* with general application to all administrative adjudication. However, a number of post-*Central Illinois* circuit court decisions apply *Dixon* without mention of *Central Illinois*. *Gulf Inland Corp. v. United States*, 570 F.2d 1277 (5th Cir. 1978), applied a Supreme Court decision retroactively which overruled an earlier circuit court decision on which the taxpayer had relied. When disallowing the taxpayer's reliance on the circuit court's decision, the *Gulf Inland* court cited *Dixon* to support the IRS's wide discretion in applying its interpretation retroactively without mention of *Central Illinois*. *Id.* at 1279.

A still later Sixth Circuit case, *Wilson v. United States*, 588 F.2d 1168 (1978), seems to want to apply *Central Illinois*, but no mention was made of it. While the issue in *Wilson* was whether or not a regulation may be applied retroactively to pending

litigation, the opinion discussed the factors limiting discretion in retroactive rule-making:

> "(1) whether or to what extent the taxpayer justifiably relied on settled prior law or policy and whether or to what extent the putatively retroactive regulation alters that law; (2) the extent, if any, to which the prior law or policy has been implicitly approved by Congress, as by legislative reenactment of the pertinent Code provisions; (3) whether retroactivity would advance or frustrate the interest in equality of treatment among similarly situated taxpayers; and (4) whether according retroactive effect would produce an inordinately harsh result."

Id. at 1173. This language suggests sympathy with the philosophy of *Central Illinois;* yet it is not cited, and *Dixon* is given great weight to result in a holding against the taxpayer.

A clarification of the scope of *Central Illinois* is important not only to the petitioner and other similarly situated foreign airlines in New York State, but also to the full range of constituents subject to administrative adjudication. The legal reality is that it is administrative agencies and not the courts that handle the majority of controversies which arise in this country each year. The potential for widespread violation of constitutional rights because of the arbitrary and capricious application of retroactive adjudication is great. A strong enunciation of the *Central Illinois* view would give form and definition to an area of administrative law that has been murky for too long.

CONCLUSION

WHEREFORE, petitioner respectfully prays that a writ of certiorari be granted.

Respectfully submitted,

s/ Robert M. Beckman
Attorney for Petitioner

APPENDIX

DENIAL OF LEAVE TO APPEAL BY THE COURT OF APPEALS DATED JUNE 5, 1979

STATE OF NEW YORK
COURT OF APPEALS

At a session of the Court, held at Court of Appeals Hall in the City of Albany on the fifth day of June A.D. 1979

PRESENT, HON. LAWRENCE H. COOKE, *Chief Judge, presiding.*

Mo. No. 417

In the Matter of Argentine Airlines,

Appellant,

Philip Ross, as Industrial Commissioner,

Respondent.

A motion for leave to appeal to the Court of Appeals in the above cause having heretofore been made upon the part of the appellant herein and papers having been submitted thereon and due deliberation having been thereupon had, it is

ORDERED, that the said motion be and the same hereby is denied.

s/ Joseph W. Bellacosa
Clerk of the Court

DENIAL OF MOTION FOR REARGUMENT AND PERMISSION TO APPEAL TO THE COURT OF APPEALS DATED MARCH 8, 1979

At a Term of the Appellate Division of the Supreme Court in and for the Third Judicial Department held at the Justice Building in the City of Albany, New York, commencing on the 17th day of November, 197 .

PRESENT:

HON. LOUIS M. GREENBLOTT
Justice Presiding

HON. MICHAEL E. SWEENEY
HON. ELLIS J. STALEY JR.
HON. ROBERT G. MAIN
Associate Justices

In the Matter of the Liability for Unemployment Insurance Contributions under Article 18 of the Labor Law of ARGENTINE AIRLINES,

Employer-Appellant

PHILIP ROSS, as Industrial Commissioner,

Respondent.

INDEX NO. 32657

A motion having been made by Argentine Airlines, employer-appellant at the above stated Term of the Court, in the above entitled proceeding, for an order granting appellant permission to reargue or in the alternative permission to appeal to the Court of Appeals from the order of affirmance entered October 2, 1978, and after reading and filing proof of due service

of the notice of motion, and no one appearing in opposition thereto, and the Court having rendered a decision on the 8th day of February, 1979, it is hereby

ORDERED, that the motion for reargument or in the alternative for permission to appeal to the Court of Appeals be and the same hereby is denied, without costs.

ENTER

DATED AND ENTERED: March 8, 1979

s/ John J. O'Brien
Clerk

A TRUE COPY
s/ John J. O'Brien
Clerk

ORDER OF AFFIRMANCE FROM THE APPELLATE DIVISION DATED OCTOBER 2, 1978

At a Term of the Appellate Division of the Supreme Court in and for the Third Judicial Department, held at the Justice Building in the City of Albany, New York, commencing on the 21st day of August, 1978.

PRESENT:

HON. LOUIS M. GREENBLOTT
Justice Presiding

HON. MICHAEL E. SWEENEY
HON. ELLIS J. STALEY JR.
HON. ROBERT G. MAIN
HON. JOHN L. LARKIN
Associate Justices

In the Matter of the Liability for Unemployment Insurance Contributions under Article 18 of the Labor Law, made by ARGENTINE AIRLINES

Employer-Appellant

PHILIP ROSS, as Industrial Commissioner,

Respondent

INDEX NO. 32657

Employer having appealed from a decision of the Unemployment Insurance Appeal Board, dated and filed in the Department of Labor, January 25, 1977, and said appeal having been submitted by both parties thereto, during the above stated

Order of Affirmance From the Appellate Division Dated October 2, 1978

Term of this Court, and, after due deliberation, the Court having rendered a decision on the 21st day of September, 1978, it is hereby

ORDER that the said decision, so appealed from, be and the same hereby is affirmed, without costs.

ENTER:

DATED AND ENTERED: Oct 2, 1978

JOHN J. O'BRIEN
Clerk

A TRUE COPY
s/ John J. O'Brien
Clerk

DECISION OF SUPREME COURT, APPELLATE DIVISION DATED SEPTEMBER 21, 1978

SUPREME COURT—APPELLATE DIVISION

THIRD JUDICIAL DEPARTMENT

September 21, 1978.

32657

In the Matter of ARGENTINE AIRLINES,

Appellant.

PHILIP ROSS, as Industrial Commissioner,

Respondent.

Appeal from a decision of the Unemployment Insurance Appeal Board, filed January 25, 1977, which modified, and affirmed, as modified, a decision of a Referee sustaining the revised determination of the Industrial Commissioner assessing the employer the sum of $14,130 as contributions due from the employer for the audit period from January 1, 1971 through December 31, 1971.

The employer is an airline organized under the laws of Argentina as a decentralized public organization to render services in the field of commercial aviation. It operates as a subdivision of a government ministry, carrying passengers and cargo on scheduled flights from Argentina to and from points in the United States, including New York, pursuant to United States Civil Aeronautics Board license. The airline employs in excess of 110 employees in New York State of which approximately one-half are Argentine nationals on assignments for the employer and one-half are United States citizens or residents.

Decision of Supreme Court, Appellate Division Dated September 21, 1978

The Appeal Board determined the employer airline to be liable for contributions and sustained a determination of the Industrial Commissioner assessing the employer the sum of $14,130 as contributions due for the 1971 calendar year.

The employer functions as a public organization within the administrative hierarchy of the government of Argentina and as a private company with respect to its commercial activities. The commercial passengers who comprise more than one-half of the employer's payload are carried at fixed rates and authorized Argentinian government employees at no charge. Argentine government cargo is carried at no charge and cargo of private concerns is carried at international airfare tariffs. In order to carry out its operations, the employer maintains an office in New York City and also leases facilities and services at John F. Kennedy International Airport. The assessment herein is based upon remuneration paid to the employees performing services in New York State.

The employer contends that since it is part of the government of Argentina, organized and operated for a public purpose, it is governmental in nature and therefore immune from liability for unemployment insurance contributions. The New York State Unemployment Insurance Law extends no express exemption from taxation to a foreign government or its operations. We conclude that by accepting a permit issued by the Civil Aeronautics Board, pursuant to 14 CFR 375.26, Argentine Airlines expressly waived, when engaged in proprietary or commercial activities, any right it might possess to assert any defense of sovereign immunity in any action or proceeding instituted against it in any court or tribunal in the United States based upon any claim arising out of operations by it under the permit. Since this claim for unemployment insurance taxes arises out of the employer's operations in New

Decision of Supreme Court, Appellate Division Dated September 21, 1978

York State, the employer should be precluded from asserting, with respect to its commercial functions, the defense of sovereign immunity as to the government of Argentina.

The record supports the determination of the board that the employer's activities are primarily commercial in nature (see *Matter of Irish Int. Airlines* [*Levine*], 48 AD 2d 202, affd. 41 NY 2d 819), and it is therefore liable for unemployment insurance contributions pursuant to article 18 of the New York State Labor Law.

Decision affirmed, without costs.

GREENBLOTT, J.P., SWEENEY, STALEY, Jr., MAIN and LARKIN, JJ., concur.

DECISION OF UNEMPLOYMENT INSURANCE APPEAL BOARD DATED JANUARY 25, 1977

NEW YORK STATE DEPARTMENT OF LABOR
Unemployment Insurance Appeal Board
Two World Trade Center
New York, N.Y. 10047

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Executive Secretary

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G. DOUGLAS PUGH
Members

E.R. #45-73201

APPEAL #223,314

REFEREE #75-31613

Argentine Airlines
9 Rockefeller Plaza
New York, New York 10020

Unemployment Insurance Bureau
Appeals & Digest
Albany, New York 12201

Lawrence W. Levine
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60 Wall Tower (70 Pine St.)
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Decision of Unemployment Insurance Appeal Board Dated January 25, 1977

PLEASE TAKE NOTICE that the decision set forth below was mailed and filed in the Department of Labor on Jan. 25, 1977.

PLEASE TAKE FURTHER NOTICE that within thirty days after the mailing of this decision, the Commissioner or any other party affected thereby who appeared at the appeal before the Board may appeal questions of law involved in such decision to the Appellate Division of the Supreme Court, Third Department. Written notice of such appeal should be mailed to the Unemployment Insurance Appeal Board, Two World Trade Center, New York N.Y. 10047, within the time above stated.

DECISION OF THE BOARD

PRESENT: Louis Sitkin James R. Rhone MEMBERS

The employer appeals from the decision of the referee filed January 16, 1976, sustaining the revised determination of the Industrial Commissioner assessing the employer the sum of $14,130 as contributions due from the employer for the audit period from the first through fourth quarters of 1971.

Hearings were held before the referee at which all parties were accorded a full opportunity to be heard and at which representatives of the employer and the Industrial Commissioner appeared and testimony was taken. The Board considered the arguments contained in the written statements submitted on behalf of the employer on appeal.

Based on the record and testimony in this case, the Board makes the following

FINDINGS OF FACT: The employer is an airline which operates as a subdivision of the Argentine Ministry of the

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Economy. It is not a corporate entity, but a public service enterprise of the government (empresa del estada). Since 1966, military personnel have flown its aircraft in Argentina and abroad. The cabin attendants are civilians. Most of the civilian personnel, who worked for the airline in this country, are United States citizens. The airline carries Argentine government personnel and mail without charge. It also carries private passengers and cargo for a fee, charging preferential rates for Argentine exports.

The New York Department of Labor requested, in letters dated January 20 and April 30, 1975, that the U.S. Department of State advise it as to whether the airline was entitled to the sovereign immunity it claimed as the government of Argentina. In its replies, dated February 25 and May 8, 1975, the State Department did not respond to this question.

OPINION: This is a case of first impression. Unlike the employers in *Matter of Irish International Airlines,* 48 AD 2d (1975), aff'g Appeal Board 183,789, and in Appeal Board 180,732, the employer herein neither is a corporation nor has it the attributes of a corporation. It is the government of Argentina. The question to be decided is whether it is, nevertheless, liable for contributions under the New York Unemployment Insurance Law, or entitled to sovereign immunity and exempt from such liability.

The American doctrine of sovereign immunity was first applied to warships in *The Schooner Exchange v. McFaddon,* 11 U.S. 116 (1812), and was extended to commercial vessels in *Berizzi Brothers Company v. S.S. Pesaro,* 271 U.S. 562, 574 (1925). Since the purpose of the doctrine is to avoid complicating foreign relations, the position of the executive branch is given some weight in deciding whether to relinquish jurisdiction, since sovereign immunity is a doctrine of judicial

abstention; but where, as here, the executive branch has taken no position, it is for the court to decide, based upon current State Department policy, whether the doctrine should be applied. *Ex Parte Peru,* 318 U.S. 578, 587-589 (1942); *Republic of Mexico v. Hoffman,* 324 U.S. 30, 34-35 (1945); *Victory Transport, Inc. v. Comisaria General,* 366 F2d 354,360 (2 Cir. 1964); *Matter of United States of Mexico v. Schmuck,* 293 N.Y. 264, 270-274 (1944). In recent years, however, the Court has been less prone to accept the State Department's position uncritically (See *National City Bank of New York v. Republic of China,* 348 U.S. 356, 361, 364 (1955); *First National City Bank v. Banco Nacional de Cuba,* 406 U.S. 759, 764, 773, 777 (1972); *Alfred Dunhill of London, Inc. v. Republic of Cuba,* 425 U.S. 682, 725 (1976).

In the interim, the State Department had adopted a "restrictive" theory of sovereign immunity in the 1952 Tate letter (text in *Dunhill,* supra, pages 711-715). The essence of this theory is that a sovereign engaged in commercial activities, normally engaged in by private persons, is, in effect, acting as a private person, and is thus liable to suit on its contractual obligations. Therefore, the employer, even though a state enterprise, would be subject to suit for a breach of contract to carry passengers or goods. *Et Ve Balik v. B.N.S. Corp.,* 25 Misc. 2d 299,303 (Sup. Ct. 1960), aff'd. 17 AD 2d 927 (1962). However, some contracts cannot be sued on because their subject matter indicates that the sovereign is acting as such and not as a private person. (*Heaney v. Government of Spain,* 445 Fed. 2d 501, 504 (2 Cir. 1971); *Aerotrade, Inc. v. Republic of Haiti,* 376 Fed. Supp. 1281, 1284-1285 (SDNY 1974). Where, as here, the sovereign could be acting both as a sovereign and as a private person, it will be immune to the extent that it is acting as a sovereign. *Pan American Tankers Corp. v. Republic of Viet-Nam,* 296 Fed. Supp. 361 (SDNY 1969).

The referee apparently based his decision on the restrictive theory of sovereign immunity, as expressed in the Tate letter. However, the Tate letter's distinction between "public acts (*jure imperii*) of a state" and "private acts (*jure gestionis*)" has been criticized as vague (*Dunhill,* supra, p. 728, n. 14; *Victory Transport,* supra, 359), and the Supreme Court has stated in *Dunhill,* supra, p. 725, that "The restrictive theory of sovereign immunity has not been adopted by this Court".

Moreover, because the Tate letter deals with contracts, it is not determinative of the question of whether a foreign sovereign is liable for unemployment contributions. Such an expansion of the restrictive theory to another field of law has recently been rejected by the Supreme Court in *Dunhill,* supra. Nor do we find controlling the Civil Aeronautics Board's regulation (14 CFR 375.26) requiring the owners and operators of foreign civil aircraft engaged in proprietary and commercial activities to waive any defense of sovereign immunity from a suit "based upon any claim arising out of operations" of such aircraft, since the regulation clearly relates to contract and tort liability.

Within the United States, the quasi-sovereign States and their subdivisions are subject to Federal taxation when engaged in commercial activities. *New York v. United States,* 326 U.S. 572, 579 (1946); *Ohio v. Helvering,* 292 U.S. 360, 369 (1934). In New York, the test for taxation of a foreign government is whether the property or activity "is used for a public' or 'governmental' purpose". *Republic of Argentina v. City of New York,* 25 NY 2d 252, 265 (1969). Accordingly, if, on balancing the employer's commercial functions (those that could be and usually are performed by private persons) against its governmental functions (those peculiar to sovereigns), the commercial aspects outweigh the governmental, then the employer is liable for contributions on all wages paid to employees of a sovereign in pursuance of such commercial

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activities. In this case, the commercial activities of the airline operated by the sovereign outweigh its governmental functions, since most of those functions could be performed by private business enterprises. This meets the criterion set forth in *New York v. United States*, supra, page 581. While some governmental purpose may be served by the operation of an airline, the operation of the airline was basically commercial and not governmental. This same reasoning was applied by the Board in finding that the operation of restaurants by a foreign country at the 1939 Worlds Fair was only incidental to its participation in the Fair for governmental purposes (Appeal Board 3962).

Our conclusion that the airline employer is liable for contributions is not based on the restrictive theory of sovereign immunity, but on the application of the test set forth in the cases cited above.

DECISION: The determination of the Industrial Commissioner is sustained.

The decision of the referee is modified accordingly, and, as so modified, is affirmed.

LOUIS SITKIN, Member
JAMES R. RHONE, Member

DECISION OF DEPARTMENT OF LABOR REFEREE DATED JANUARY 16, 1976

NEW YORK STATE DEPARTMENT OF LABOR
Unemployment Insurance Referee Section
Two World Trade Center
New York, N.Y. 10047

IRVING WIENER
JOSEPH N. FRISTACHI
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AARON N. FEDER
Chief Referee

In the Matter of:

Argentine Airlines
9 Rockefeller Plaza
New York, New York 10020

Referee #75-31613

E.R. #45-73201

DECISION MAILED AND DULY FILED IN THE DEPARTMENT OF LABOR ON JANUARY 16, 1976

HRG. REP. UNIT BLDG.
ATT: Joseph Victory

New York State Dept. of Labor
Unemployment Insurance Division
State Office Building Campus
Albany, New York 12201
Att: Appeals and Digest Unit

Decision of Department of Labor Referee Dated January 16, 1976

Lawrence W. Levine
Walsh & Levine
60 Wall Tower (70 Pine Street)
New York, New York 10005

FINDINGS OF FACT: Hearings were held at which the employer's attorney and a representative of the Industrial Commissioner appeared and testified.

On December 30, 1974, a determination was issued assessing the sum of $14,100 as revised, against the employer for contributions due for the audit period January 1, 1971, to December 31, 1971.

The employer herein is an *empresa del estado* of a foreign government, that is, it is an integral department of that government. It operates an airline carrying passengers and freight in international commerce between Argentina and other countries, including the United States. Since before January 1, 1971, it has maintained offices in New York City and facilities at John F. Kennedy International Airport in Queens, New York. It had, in 1971, approximately 110 employees and freight without charge, the bulk of its passengers and a large amount of its freight is commercial in character for which fares are charged and freight charges are collected. Its employees in New York are government employees and are primarily office personnel. They are members of a union which is in contractual relations with the airline employer. Maintenance of airplanes is contracted for. By treaty with United States, the airline employer is not required to pay taxes on income realized from sources within the United States. Under the Federal Unemployment Tax Act, the employer is not required to pay taxes because its employees are government employees. The employer has been granted exemption from New York State and City sales taxes. The

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amount determined to be due was based on an estimate because of the employer's refusal to submit to an audit prior to determination of liability.

OPINION: The issue presented is whether an airline operated as an integral part of a foreign government for both governmental and commercial purposes should be deemed liable for contributions as an employer under the New York State Unemployment Insurance Law. The employer contended that, as a part of the government, the employing airline was carrying out a public purpose, that is jure imperium, as opposed to a commercial purpose, or jure gestionis, and, therefore, should be exempt from unemployment insurance contributions under the New York Law. The issue involves considerations of international law. It may be noted that Section 560.1 of the Law makes an employer liable for contributions if the employer has paid remuneration of $300, or more, in any calendar quarter. It has been held that a foreign government instrumentality, an airline, is not exempted from contributions under the law by Section 560.4 which exempts municipal corporations and other governmental subdivisions as employers liable for contributions under the article. Because of its derivation, that section relates to State, city, county and local entities, not to a foreign government. Nor is the employing airline entitled to exemption because of the fact that it has been granted exemptions under other taxing statutes of the State. Section 560.5 of the Law precludes such a result. Unlike the Federal Unemployment Tax Act and, for example, the California Unemployment Insurance Code, there is no exemption in the New York Law with respect to a foreign government, or an instrumentality thereof.

The Income Tax Treaty between the United States and the airline employer's government does not preclude liability under the New York State Law. The tax under the Unemployment Insurance Law is not a tax on income; it is a tax on wages paid to employees.

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It was contended on behalf of the employer that the airline's operation was for a public purpose. Had it been operated exclusively by government employees, solely for the purpose of transportation of government employees and government property, the contention might have been well founded. However, the operation was primarily commercial in nature, dependent in large part on the fares and freight charges which it collected from non-government travellers and in respect of non-government property. That it was subsidized by government appropriations and even that it operated at a loss did not change the commercial character of its operation. Rather, it is apparent that the commercial operations contributed greatly to the ability of the government to maintain the service. In essence then, notwithstanding the public purpose which the airline served, it was a commercial operation and, therefore, should be treated as such and in the same manner as any other airline employer having employees in New York.

In *Matter of Irish International Airlines,* 48 A.D. 202, the court affirmed a decision of the Appeal Board, AB 183,789, holding that an airline wholly owned by a foreign government was subject to contributions to the New York State Unemployment Insurance Fund. In Appeal Board #180,732, the appeal board affirmed a decision holding that an airline operated as an instrumentality of a foreign government was liable for contributions to the New York State Unemployment Insurance Fund. So far as the requirements of the New York Law are concerned, there is no distinction between the airlines in those cases and that in this case.

Accordingly, the employer was subject to the Unemployment Insurance Law in the audit period involved. The matter is referred to appropriate authority for determination of the amount due.

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DECISION: The determination of liability is sustained.

s/ JOHN HOLBROOK
Referee

IF YOU ARE STILL UNEMPLOYED, CONTINUE TO REPORT TO PROTECT YOUR RIGHTS.

NOTICE OF DECISION

Please take notice that as a result of a hearing held before an Unemployment Insurance Referee, the aforementioned decision was made, and has been duly filed in the Department of Labor on the date listed on the face of the decision.

Take further notice that if you are not satisfied with the decision, you may appeal to the Unemployment Insurance Appeal Board. Such appeal should be directed to the Department of Labor, U.I. Accounts Bureau, Appeals and Digest Section, State Office Building Campus, Albany, New York 12201 stating that you wish to appeal from this decision, and stating the reasons for such appeal. The appeal may be made in person or by writing, AND MUST BE TAKEN WITHIN TWENTY (20) DAYS AFTER THE MAILING DATE OF THE DECISION.

AB 585 (3-73)